REMARKS

This is in response to the Official Action mailed on March 28, 2003.

Claims 1-12, 16-18, and 21-33 are pending in this application. The Office Action Summary refers to claims 1-31, but the detailed action makes clear that the Examiner has reviewed original claim 32.

To expedite prosecution, the subject matter of claims 13-15 and of claims 19-20 have been presented in independent claims and claim 32 has been amended. Applicants reserve the right to present broader claims in a continuing application.

Objections

The Specification was objected to due to an informality which has been corrected by this Amendment.

Claims 19, 29, and 32 were objected to due to informalities which have been attended to in this amendment by deleting an extraneous word. Applicants believe the Examiner's comments were directed to claims 19, 28 and 32, and have made amendments accordingly. The Examiner comments in this regard were instructive and withdrawal of this objection is believed to be warranted.

The Section 102 Rejection

Claims 1-32 stand rejected as anticipated by Kolb, "Futures, Options, and Swaps, Third Ed., 1999" ("Kolb"). The Examiner refers to several chapters in this document in formulating his rejection of the pending claims. Applicants respectfully traverse this rejection and state that the portions of Kolb that were cited in the Office Action fail to teach or suggest the methodology of the amended claims.

Applicants have carefully reviewed the portions of Kolb provided by the Examiner and submit that Kolb fails to teach or suggest **volatility arbitrage** as that term is defined in the pending claims. Rather, the **index arbitrage** of Kolb invokes an analysis of the value of stock prices or physical commodities (such as soy beans) verses a corresponding futures price in the same sector.

Kolb describes several index arbitrage methodologies. In table 7.8, index futures are sold against long positions in a stock. In table 7.9, stock is sold short while index futures are bought. These examples show a one-for-one correspondence between stock and index positions, and lack a tracking basket which emulates an underlying index by containing only a segment of instruments in the underlying index. Kolb explains that with the use of computers, such one-for-one trading can be achieved with indices such as the S&P 500 which requires the buying and selling of 500 different securities. Critically, Kolb fails to recognize or suggest the establishment or use of a tracking basket which includes equities having high volatility that can be hedged to raise monies, nor does Kolb even suggest at an option strategy in which a tracking basket is hedged through the purchase of puts on an index coupled with the sale of

calls on individual equities in the tracking basket in order to "raise premium in an amount greater than the cost of buying the put options."

With respect to amended claim 1, the dynamic hedging step operates upon a tracking basket which is a concept not addressed by Kolb. Moreover, the claimed methodology departs radically from the one-for-one correspondence described in Kolb by implementing a strategy in which call options are sold against tracking basket components in order to a raise premium "in an amount greater than the cost of buying the put options" which, in turn , is in "an amount sufficient to cover the notional amount of the tracking basket." In sharp contrast, Kolb has put options to cover the notional amount of an entire index, and fails to recognize that the cost of buying the put option can be fully recovered through the selective sale of calls on stocks in a tracking basket.

With regard to claim 32, the Examiner contends that the claimed actions of the computer program are known from Kolb, but Applicants respectfully submit that, while it is true that Kolb purports to provide a software program to compute the options and swaps discussed in his text, Kolb nevertheless fails to disclose or even suggest the actions recited in this claim. The Examiner refers to chapter 7 in support of this rejection, but Applicants respectfully note that the discussion of stock index futures contracts and index arbitrage merely address perceived disparities between future prices and the fair value of the stock; there is no recognition of the program of claim 32 in which there is a tracking basket, in which there are different sets of options identified which having "a relative implied volatility which is greater than its historical volatility in a given maturity period," or of any balancing of "the implied

volatility percentage of the options in the first set against the relative implied volatilities of the options in the second set to identify a selection of options to sell." Neither do Applicants see any teaching or suggestion of the step of "identifying one or more put options which, together with the selection of options to sell, results in a net delta of a portfolio which includes the tracking basket, the selection of options to sell, and the identified put options which is below a threshold value." The claimed software program results in the identification of "a generally risk neutral portfolio," yet Applicants see no teaching of such a program in Kolb.

For that matter, Applicants question the basis in Kolb for the contention that it anticipates the subject matter of claims 10 and 11. These claims call more specifically for a tracking basket that includes less than a predetermined percentage (such as 70%) of the underlying index. Kolb describes the hedging of a physical inventory using futures contracts, and has a computation of the percentage of that inventory to hedge with such contracts. However, this teaching has no bearing at all on how one goes about constructing a tracking basket, the subject matter of these claims.

With respect to new claim 33, the distinction over Kolb is more compelling, as new claim 33 calls for a specific analyses against the components in the tracking basket to arrive at a hedging operation in which the purchasing of a long put against the underlying index is "for an amount which is not substantially greater than the premium raised" through the selling of a selection of options against the components in the tracking basket.

The difference between the volatility of the underlying index and the individual volatilities of stocks that have been included in the tracking basket provides a foundation for an

account that is to be actively managed. Kolb does not recognize such an account building technique, and instead focuses on strategies to arbitrage perceived differences between present and future values. However, by establishing a tracking basket and purchasing selected puts on the index to which the tracking basket correlates, and then by selling calls on specific constituents in tracking basket to raise premium to cover the cost of the put, the claimed methodology takes advantage of the volatility differences between the index and the tracking basket components to permit an account to be hedged and a profit to be made. This establishes a smooth return flow and allows for a return that is most cases should be less volatile than the underlying index.

Respectfully submitted,

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